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SUBJECT: NEPAL: ECONOMIC HIGHLIGHTS FOR THE MONTH OF
FEBRUARY 2009

REF: KATHMANDU 158

11. (U) Below is a compilation of economic highlights from
Embassy Kathmandu for the month of February 2009, including
the following:

- Remittance Growth Through December, Expected To Fall In
2009
- Government Revenues Increase
- Government Spending Down
- Inflation Remains High
- Trade Continues To Grow
- Electricity Crisis Deepens

Remittance Growth Through December, Expected To Fall In 2009

12. (U) Nepal Rastra Bank (NRB), Nepal's central bank,
reported in early February that worker remittances to Nepal
increased 66 percent in the first five months of fiscal year
(FY)09 (July 15-December 15) compared to the same period last
year. However, the deepening global recession will likely
slow remittance growth in the coming months; predictions in
the local press reach as high as 40 percent. On January 25,
the Malaysian government announced a suspension of new work
permits for foreign workers, halting the roughly 3,500
Nepalese who leave for Malaysia each month. As remittances
contributed \$2.2 billion to the FY08 budget (15.5 percent of
GDP), a potential influx of unemployed workers returning to
Nepal would likely negatively affect the balance of payments
and increase social and economic pressures on Nepal's
domestic economy.

Government Revenues Increase

13. (U) Government revenue collection increased 32.5 percent
to 72.26 billion Nepali Rupees (NRs) (approximately \$963
million at an exchange rate of NRs 75 to the dollar) over the
first seven months of FY09 (July 15-February 15) against NRs
54.52 billion (\$727 million) in the same period last year.
The government aims to increase revenue collection to meet
the budgetary target of NRs 142 billion (\$1.9 billion). The
Voluntary Declaration of Income Scheme, an initiative in this
year's budget that encourages non-taxpayers to legalize their
assets and avoid penalties, collected NRs 1.04 billion (\$14
million) by mid-February and drove revenue growth along with
VAT collection, import duties, excise tax, and vehicle tax

and registration fees.

Government Spending Down

¶4. (U) The budget remained at a NRs 2.2 billion surplus (\$29 million) in the first five months of FY09 compared to a NRs 9.8 billion deficit (\$131 million) in the corresponding period last year. Total government spending in both recurrent and capital spending declined. While recurrent spending declines can be partially attributed to large election expenditures in 2008, the Government of Nepal has not explained the 34 percent decrease in capital expenditures (compared to a 120 percent increase in the first 5 months of FY08). Despite a higher development budget this fiscal year, development spending is down 23 percent in the first 6 months of FY09 (July 15-January 15) over last year. On January 19, Finance Minister Spokesperson Shankar Adhikari attributed the slow spending to the late release of the budget (in September instead of July) and claimed that spending would pick up now that procedural matters are complete.

Inflation Remains High

¶5. (U) The World Food Programme announced on February 12 that Nepal's inflation rate stood at 14.4 percent, according to their own study. NRB reported in early February that year-on-year inflation stood at 14.1 percent in mid-December compared to 5.7 percent a year ago. Soaring prices of food and beverages contributed most to inflation at 17.2 percent

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(7.1 percent a year ago). As a response to high food prices in Nepal despite falling international prices, the Ministry of Commerce and Supplies announced on February 24 that they will distribute rice, wheat flour, cooking oil, ghee, and pulses (legumes) at fair prices through its network of supply outlets. Non-food and services inflation stood slightly lower at 10.8 percent (4.1 percent a year ago). Regionally, Kathmandu faced the highest inflation at 16.2 percent (4.9 percent a year ago) followed by the Hills at 13.6 percent (5.3 percent a year ago) and the Terai at 13.1 percent (6.2 percent a year ago).

Trade Continues To Grow

¶6. (U) Exports rose 30.9 percent in the first five months of FY 08/09 compared to a 4.4 percent decline last year, according to NRB. Exports to India rose 15.1 percent (9 percent decline a year ago) and exports to other countries rose 64 percent (6.9 percent increase a year ago). Revenue from export growth partially financed the 32.6 percent increase in imports (8.2 percent increase a year ago). Imports from India rose 17.1 percent (10.7 percent a year ago) and imports from other countries rose 57.2 percent (4.5 percent a year ago). The rapid increase in imports from countries other than India consisted largely of gold, steel, machinery parts, and computer equipment. The U.S. ran a \$2.8 million trade deficit with Nepal for the month of December (\$5.3 million in December 2007), and a \$56.3 million deficit in 2008 (\$61 million in 2007); the U.S. trade deficit with Nepal has decreased yearly since 2003.

Electricity Crisis Deepens

¶7. (U) Nepal's daily power cuts (load shedding) reached 16 hours per day in February due to demand for power that outweighed domestic generation and import capacity. Load shedding significantly increases business costs because expensive generators and fuel must be used. The Nepal Electricity Authority (NEA) announced February 24 that Nepal will import 50-60 megawatts (MW) from India through the Koshi-Kattaiya transmission line in the Sunsari district,

formally out of service since August 2008 when floods destroyed towers in India and Nepal. The new power source will likely provide little consumer relief as the NEA plans on shutting down the 46MW Kulekhani Reservoir power plant once imports begin. In early February, the Kulekhani plant was used 24 hours per day, resulting in a five meter water loss in the reservoir; only 10-11 meters remain that could generate power, according to NEA's System Maintenance and Operation Department Director Sher Singh Bhat. Nepal currently produces about 260MW of power and demands roughly 700MW.

Comment

18. (SBU) To date, impacts of the global financial crisis and worldwide recession have not affected remittance growth, and inflation may finally be leveling off, good news for a struggling economy. However, preliminary reports of overseas workers returning home from lost jobs, a power crisis with no resolution in sight, and continued high prices for a range of goods threaten Nepal's ability to achieve substantial economic growth in 2009.

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